In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 109

GIRARD TRUST CORN EXCHANGE BANK, AS TRUSTEE OF A TRUST UNDER DEED OF ALBERT R. GALLATIN WELSH DATED MARCH 19, 1935, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 15a-20a) is reported at 16 T.C. 1398. The opinion of the Court of Appeals (R. 22-23) is reported at 194 F. 2d 708.

JURISDICTION

The judgment of the Court of Appeals was entered on February 27, 1952. (R. 23.) Petition for rehearing was denied March 25, 1952. (R. 24.) The petition for a writ of certiorari was filed on June 7,

1952. The jurisdiction of this Court is invoked under 28 U.S.C. 1254 (1).

QUESTION PRESENTED

In 1948 petitioner made a payment of trust principal to a divorced wife of a deceased husband to satisfy arrears in payments of his legal obligation under a separation agreement and divorce decree. The question presented is whether the payment constituted income to the divorced wife under Section 22 (k) of the Internal Revenue Code.[1]

STATUTE AND REGULATIONS INVOLVED

The pertinent statute and Treasury Regulations are set forth in the Appendix, *infra,* pp. 12-20.

STATEMENT

The facts were stipulated (R. 3a-14a) and were found by the Tax Court as stipulated (R. 15a-16a). They may be restated as follows:

The taxes in controversy are income taxes for the calendar year 1948 in the amount of $5,400 for which the Commissioner determined that the Girard Trust Company is liable as withholding agent with respect to amounts paid to Gabrielle B. Welsh. The Girard Trust Company was one of the trustees of a trust under deed of Albert R. Gallatin Welsh dated March 19, 1935, and as such trustee had pos-

[1] Another question raised in the courts below—whether the payments constituted "fixed or determinable annual or periodical" income within the meaning of Sections 143 (b) and 211 (a) (1) (A) of the Internal Revenue Code (26 U.S.C. 1946 ed., Secs. 143 and 211) so as to be taxable to the recipient as a nonresident alien and subject to withholding tax by petitioner—has apparently been abandoned by petitioner.

session and custody of the funds of such trust. (R. 3a.) The name of the corporation was apparently changed to Girard Trust Corn Exchange Bank effective June 15, 1941.[2] (For convenience the corporation will herein be called either the "Girard Trust Company" or the "petitioner".)

Gabrielle B. Welsh and Albert R. Gallatin Welsh were married on October 25, 1933, in Paris, France. There were no children of the marriage. (R. 3a.)

On March 19, 1935, Albert created a trust of which the Girard Trust Company and Charles N. Welsh, Jr., were and still are co-trustees. Under the trust Albert reserved a power of appointment by will. (R. 4a.)

On May 16, 1938, Albert and Gabrielle entered into a separation agreement and in the same year, effective December 20, 1938, they were divorced by an adjudication of the District Court of Zurich, Switzerland. (R. 3a-4a.) The separation agreement (R. 7a-9a), while providing that it should in no wise be affected by divorce, nevertheless provided that Albert should pay Gabrielle $400 per month until her death or remarriage. The decree of divorce (R. 11a) did not refer to the agreement but did require Albert to pay Gabrielle, in advance, for her support the sum of $400 per month until her remarriage. Gabrielle never remarried. (R. 4a.)

Albert subsequently remarried. He died December 1, 1944, a resident of Delaware County, Penn-

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[2] It is so alleged in the petition for review by the Court of Appeals.

sylvania. At all times he was a citizen of the United States. He was survived by his second wife, Helene, and two sons of his second marriage. (R. 4a.)

Albert left a last will and testament dated November 18, 1940, which was duly admitted to probate by the Register of Wills of Delaware County, Pennsylvania, of which will the Girard Trust Company and Charles N. Welsh, Jr., brother of the decedent, are executors. The will made no provision for Gabrielle. By Article Second of the will Albert exercised his power of appointment over the trust dated March 19, 1935 (R. 4a), by directing payment of one-half of the trust income to Helene, his second wife, and the remainder of the income to his children (R. 12a).

Albert's net estate, exclusive of property held in the March 19, 1935, trust, amounted to $1,471.29 after paying claims other than that of Gabrielle B. Welsh. (R. 4a-5a.)

Gabrielle instituted proceedings in the Orphans' Court of Philadelphia County, Pennsylvania, which had jurisdiction of the trust under deed dated March 19, 1935, to subject the corpus of the trust to her claim as a creditor of the estate for the payment of $400 per month, pursuant to the separation agreement and the divorce decree referred to above. The Orphans' Court of Philadelphia County entered a supplemental adjudication dated October 1, 1947 (R. 13a-14a), in which it awarded to Gabrielle from the principal of the

trust the total amount of all unpaid monthly sums of $400 accruing from the date of Albert's death and payments at the rate of $400 per month to be paid thereafter pursuant to the provisions of the separation agreement and the divorce decree. There was no appeal from such adjudication and the adjudication became final on the expiration of the time allowed for an appeal (R. 5a.)

Since Albert's death the trustees have paid the trust income regularly each year, including 1948, to the beneficiaries appointed by Albert in his will, namely, one-half to Helene Welsh, his second wife, and one-half in equal shares to their two children. Such income for the year 1948 was reported for federal income tax purposes by such beneficiaries. Albert's estate had no income in 1948. (R. 5a.)

Pursuant to the provisions of the adjudication of the Orphans' Court of Philadelphia County, dated October 1, 1947, the Girard Trust Company, as trustee, in 1948 set aside the sum of $18,000 from the principal of the trust to satisfy payments at the rate of $400 a month due Gabrielle B. Welsh subsequent to Albert's death. Of that amount, the Girard Trust Company paid Gabrielle $12,600 in 1948, and retained the balance of $5,400 to cover liability, if any, for withholding tax at the rate of 30 percent on such sum of $18,000. (R. 5a-6a.)

At all times referred to herein and at the time of the hearing, Gabrielle was a nonresident alien

of the United States and a citizen of France. Her residence at the present time is at Saigon, French Indo-China. She was not at any time during 1948 engaged in trade or business within the United States. (R. 6a.)

On these facts, the Tax Court held that the 1948 payment of trust principal to Gabrielle constituted income to her within the meaning of Section 22 (k) of the Internal Revenue Code and that, since such income is taxable to a nonresident alien under Section 211 (a)(1) and subject to withholding tax under Section 143 (b), petitioner, as withholding agent, is liable for the withholding tax on such income. (R. 15a-20a.) The Court of Appeals affirmed for the reasons stated in the Tax Court's opinion. (R. 22.)

ARGUMENT

The petitioner argues that the decision below is incorrect and presents an important question as to which the state of the law is confused (Pet. 4-9; Br. 23-27). We submit the decision below is patently correct and there is no present confusion in respect of the question presented by the petition.

1. Gabrielle B. Welsh, who was divorced from Albert R. Gallatin Welsh in 1938, is taxable under Section 22 (k) of the Internal Revenue Code (Appendix, *infra*, p. 12) on "periodic payments" (whether or not made at regular intervals) received by her subsequent to the divorce decree in discharge of a legal obligation which, because of the

marital relationship, was imposed upon and incurred by Albert under their separation agreement and divorce decree.[3] Petitioner does not and cannot deny that the payment of trust principal it made to Gabrielle Welsh in 1948, having been made to satisfy arrears of payments at the rate of $400 a month due Gabrielle subsequent to her former husband's death, constituted "periodic payments" within the meaning of the statute and was made "in discharge of" her former husband's legal obligation under the separation agreement and divorce decree. Section 22 (k) covers such payments even though they are made after the husband's death. See *Fairbanks* v. *Commissioner,* 191 F. 2d 680 (C.A. 9th); *Laughlin's Estate* v. *Commissioner,* 167 F. 2d 828 (C.A. 9th); *Izrastzoff* v. *Commissioner,* 193 F. 2d 625 (C.A. 2d).

Petitioner's contention that Section 22 (k) is nevertheless inapplicable here is based primarily upon a distortion of the parenthetical clause contained at the end of Section 22 (k). (Br. 12-14.) Petitioner interprets that clause as making Section 22 (k) inapplicable and Section 171 (a) (Appendix, *infra,* p. 13) applicable to any payment attributable to property of an estate or to property

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[3] Petitioner's liability is as withholding agent of fixed or determinable annual or periodical income paid to Gabrielle Welsh, a nonresident alien. See Sections 143 (b) and 211 (a) (1) (A) of the Code (26 U.S.C. 1946 ed., Secs. 143 and 211). The court below affirmed the Tax Court's holding that the lump sum payment involved here constituted fixed or determinable annual or periodical income (R. 22) and petitioner now contends only that the payment was not taxable income to Gabrielle Welsh under Section 22 (k).

held in trust, and accordingly argues that, since Section 171 (a) taxes only trust income, Gabrielle Welsh is not taxable on the trust principal paid her in 1948. (Pet. 5-6; Br. 11-14.) Petitioner's error is in confusing paragraphs (a) and (b) of Section 171. The parenthetical clause at the end of Section 22 (k) refers only to paragraph (b) of Section 171, which is not a taxing provision. The parenthetical clause was inserted by Congress merely to make it clear, for the purpose of the provisions of the Code taxing income of a trust or estate to the beneficiary and allowing the trust or estate a deduction therefor (see Section 162 of the Code, 26 U.S.C. 162), that the wife is a beneficiary as to that part of any periodic payment, required by Sections 22 (k) or 171 (a) to be included in the income of the wife which is a distribution of income of a trust or estate. See S. Rep. No. 1631, 77th Cong., 2d Sess., p. 85 (1942-2 Cum. Bull. 504, 569). Section 171 (a), which petitioner attempts to substitute for Section 171 (b), covers a situation not covered by Section 22 (k) and was specifically intended by Congress to apply to a situation "to which the provisions of section 22 (k) are not applicable" (S. Rep. No. 1631, *supra,* p. 85), rather than to supplant Section 22 (k) respecting payments from a trust of the type designated in Section 22 (k). (See Treasury Regulations 111, Section 29.171-1, Appendix, *infra,* pp. 17-20.) No distinction is drawn in Section 22 (k) as between payments from income and capital, or between payments from trust income and trust prin-

cipal, and the language of the statute is broad enough to cover any such payments, providing they satisfy the requirements of the section. That Congress did not intend that any distinction should be drawn in respect of the source of the payments, whether from income, capital, trust income, or trust principal, is so clear as to be beyond question. See S. Rep. No. 1631, *supra,* pp. 84-85. See also, Treasury Regulations 111, Section 29.22(k)-1 (Appendix, *infra,* pp. 14-15).

2. The decisions relied upon by petitioner to show inconsistency or confusion in the state of the law in respect of the question here presented (Pet. 6-9; Br. 23-27) are entirely consistent with the decision below. In *Laughlin's Estate* v. *Commissioner,* 167 F. 2d 828 (C.A. 9th), a property settlement agreement later incorporated into the divorce decree provided for monthly payments by the husband to the wife for her life. After the husband's death, his estate made the payments to the wife and the question was whether the estate was entitled to a deduction therefor. The affirmative holding of the Ninth Circuit was based upon the conclusion that the payments (which may have been made from principal rather than from income) were covered by Section 22 (k), the fact that under Section 171 (b) the wife was to be considered a beneficiary as to payments described in Section 22 (k), and the fact that under Section 162 (b) (26 U.S.C. 162) the estate was entitled to a deduction for currently distributable amounts to the extent of the distributable income of the estate,

whether or not actually paid from income. *Fairbanks* v. *Commissioner,* 191 F. 2d 680 (C.A. 9th), stands for the proposition that payments which were made to the wife from a trust, after the husband's death, were constitutionally taxable income to the wife under Section 22 (k). The holdings in these two cases that the payments involved were covered by Section 22 (k) is consistent, rather than inconsistent, with the decision below.[4] The statement in the *Fairbanks* case referred to by taxpayer (Br. 23)—that the same court's decision in the *Laughlin's Estate* case was not intended to permit a diminution of tax on the estate of the husband without sanctioning a corresponding liability of the wife—means only what it says and not, as taxpayer intimates (Br. 23-24), the converse. *Estate of Reid* v. *Commissioner,* 15 T.C. 573, affirmed *sub nom. Izrastzoff* v. *Commissioner,* 193 F. 2d 625 (C.A. 2d), involved a situation and holding similar to the *Laughlin's Estate* case, *supra,* as taxpayer's explanation of the case shows (Br. 24). *Stewart* v. *Commissioner,* 9 T.C. 195, involved tax-exempt trust income, whereas the trust principal received by petitioner is taxable under Section 22 (k).

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[4] It is petitioner who is inconsistent. On the merits it attempts to ignore the fact that the reference in the parenthetical clause at the end of Section 22 (k) is to paragraph (b) of Section 171, rather than to paragraph (a), and then, on the other hand, it asserts that the decision below is contrary to the reasoning in the *Laughlin's Estate* decision because that decision held that paragraph (b) of Section 171 is applicable to Section 22 (k) payments.

CONCLUSION

The decision below is correct and involves no conflict of decisions. The petition for a writ of certiorari should therefore be denied.

Respectfully submitted,

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JULY, 1952.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

* * * * *

(k) [As added by Sec. 120 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Alimony, Etc., Income.*—In the case of a wife who is divorced or legally separated from her husband under a decree of divorce or of separate maintenance, periodic payments (whether or not made at regular intervals) received subsequent to such decree in discharge of, or attributable to property transferred (in trust or otherwise) in discharge of, a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce or separation shall be includible in the gross income of such wife, and such amounts received as are attributable to property so transferred shall not be includible in the gross income of such husband. * * * (In cases where such periodic payments are attributable to property of an estate or property held in trust, see section 171 (b).)

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(26 U.S.C. 1946 ed., Sec. 22.)

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(u) [As added by Sec. 120 (b) of the Revenue Act of 1942, *supra*] *Alimony, Etc., Payments.*—In the case of a husband described in section 22 (k), amounts includible under section 22 (k) in the gross income of his wife, payment of which is made within the husband's taxable year. If the amount of any such payment is, under section 22 (k) or section 171, stated to be not includible in such husband's gross income, no deduction shall be allowed with respect to such payment under this subsection.

* * * * *

(26 U.S.C. 1946 ed., Sec. 23.)

SEC. 171 [As added by Sec. 120 (c) of the Revenue Act of 1942, *supra*] INCOME OF AN ESTATE OR TRUST IN CASE OF DIVORCE, ETC.

(a) *Inclusion in Gross Income.*—There shall be included in the gross income of a wife who is divorced or legally separated under a decree of divorce or of separate maintenance the amount of the income of any trust which such wife is entitled to receive and which, except for the provisions of this section, would be includible in the gross income of her husband, and such amount shall not, despite section 166, section 167, or any other provision of this chapter, be includible in the gross income of such husband. * * *

(b) *Wife Considered a Beneficiary.*—For the purposes of computing the net income of the estate or trust and the net income of the wife described in section 22 (k) or subsection

(a) of this section, such wife shall be considered as the beneficiary specified in this supplement. A periodic payment under section 22 (k) to any part of which the provisions of this supplement are applicable shall be included in the gross income of the beneficiary in the taxable year in which under this supplement such part is required to be included. (26 U.S.C. 1946 ed., Sec. 171.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.22(k)-1. *Alimony and separate maintenance payments—Income to former wife.*—(a) *In general.*— * * *

(b) *Alimony income attributable to property.*—The full amount of periodic payments received under the circumstances described in section 22 (k) is required to be included in the gross income of the recipient whether such amounts are derived, in whole or in part, from income received or accrued by the source to which such payments are attributable. Thus, it matters not that such payments are attributable to property in trust, to life insurance, endowment, or annuity contracts, or to any other interest in property, or are paid directly or indirectly by the obligor husband from his income or capital. For example, if in order to meet an alimony obligation of $500 a month, the husband purchases or assigns for the benefit of his former wife a commercial annuity contract paying such amount, the full $500 a month received by the wife is includible in her income, and no part

of such amount is includible in the husband's income or deductible by him. See section 22 (b)(2)(A) and section 29.22(b)(2)-4. Likewise, if property is transferred by the husband, subject to an annual charge of $5,000, payable to his former wife in discharge of his alimony obligation under the divorce decree, the $5,000 received annually is, under section 22 (k), includible in the wife's income, regardless of whether such amount is paid out of income or principal of the property.

The same rule applies to periodic payments attributable to property in trust. The full amount of periodic payments to which section 22 (k) applies is includible in the wife's income, regardless of whether such payments are made out of trust income. This rule applies even though under the law applicable to taxable years beginning before January 1, 1942, only the income of a trust for the benefit of the divorced wife was taxable to her. Such periodic payments are to be included in the wife's income under section 22 (k) and are to be excluded from the husband's income, even though the income of the trust would otherwise be includible in his income under section 22 (a), section 166, section 167, or any other section of the Code or these regulations. As to periodic payments received by a former wife attributable to property in trust in cases to which section 22 (k) does not apply because the husband's obligation is not specified in the decree or an instrument incident thereto, see section 171 (a) and section 29.171-1.

* * * * *

SEC. 29.23(u)-1. *Periodic alimony payments.*— * * *

The deduction under section 23 (u) is allowed only to the obligor spouse. It is not allowed to an estate, trust, corporation, or any other person who may pay the alimony obligation of such obligor spouse. The obligor spouse, however, is not allowed a deduction for any periodic payment includible under section 22 (k) in the income of the wife or former wife, as the case may be, which payment is attributable to property transferred in discharge of his obligation and which, under section 22 (k) or section 171 is stated not to be includible in his gross income.

The following examples illustrate cases in which a deduction is or is not allowed under section 23 (u):

* * * * *

Example (2). A decree of divorce obtained by W from H incorporated a previous agreement of H to establish a trust, the trustees of which were instructed to pay W $5,000 a year for her life. The court retained jurisdiction to order H to provide further payments if necessary for the support of W. In 1942 the trustees paid to W $4,000 from the income of the trust and $1,000 from the corpus of the trust. Under the provisions of sections 22 (k) and 171 (b), W will include $5,000 in her income for 1942. (The trustees will deduct $4,000 from the income of the trust under section 162.) H will not include any part of the $5,000 in his income nor take a deduction

therefor. If H had paid the $1,000 to W, rather than allowing the trustees to pay it out of corpus, he would have been entitled to a deduction for $1,000 under the provisions of section 23 (u).

* * * * *

SEC. 29.171-1. *Income of trust in case of divorce, etc.*—(a) *In general.*—Section 171 (a) provides rules in certain cases for taxability of income of trusts as between spouses who are divorced or legally separated under a court order or decree. In such cases, the spouse actually entitled to received payments from the trust is considered the beneficiary rather than the spouse in discharge of whose obligation such payments are made. For convenience, the beneficiary spouse will hereafter in this section and in section 29.171-2 be referred to as the "wife" and the obligor spouse from whom she is divorced or legally separated as the "husband". * * * Thus, under section 171 (a) income of a trust—

(1) which is paid, credited or to be distributed to the wife in a taxable year of the wife, and

(2) which, except for the provisions of section 171, would be includible in the gross income of her husband,

shall be includible in her gross income and shall not be includible in his gross income.

Section 171 (a) does not apply in any case to which section 22 (k) applies. Although section 171 (a) and section 22 (k) seemingly

cover some of the same situations, there are important differences between them. Thus, section 171 (a) applies, for example, to a trust created before the divorce or separation and not in contemplation of it, while section 22 (k) applies only if the creation of the trust or payments by a previously created trust are in discharge of a legal obligation imposed upon or assumed by the husband (or made specific) under the court decree or an instrument incident to the divorce or legal separation. On the other hand, section 22 (k) requires inclusion in the wife's income of the full amount of periodic payments received attributable to property in trust (whether or not out of trust income), while section 171 (a) requires amounts paid, credited or to be distributed to her to be included only to the extent such amounts are out of income of the trust for its taxable year (determined as provided in section 162).

Section 171 (a) is designed to produce uniformity as between cases described in section 171 (a) and cases not described in section 171 (a), where, in the former cases, without section 171 (a), the income of a so-called alimony trust would be taxable to the husband because of his continuing obligation to support his former wife, and where, in the latter cases, the income of a so-called alimony trust is taxable to the former wife because of the termination of the husband's obligation. Furthermore, section 171 (a) taxes trust income to the wife in all cases where under prior law the hus-

band would be taxed not only because of the discharge of his alimony obligation but also because of his retention of control over the income or trust corpus. Section 171 (a) applies whether or not the wife is the beneficiary under the terms of the trust instrument or is an assignee of a beneficiary.

The application of section 171 (a) may be illustrated by the following examples, in which it is assumed that both the husband and wife make their income tax returns on a calendar year basis:

Example (1). Upon the marriage of H and W, H irrevocably transfers property in trust to pay the income therefrom to W for her life for support, maintenance, and all other expenses. Some years later, W obtains a legal separation from H under an order of court. W, relying upon the income from the trust payable to her, does not ask for any provision for her support and none is ordered by the court; the court, however, has jurisdiction under the law of the State to order at any time prior to an absolute divorce that provision be made by H for W's support. Under the provisions of section 171 (a), the income of the trust which becomes payable to W after the order of separation is includible in her income and is deductible by the trust. No part thereof is includible in H's income or deductible by him.

Example (2). H transfers property in trust for the benefit of W, retaining the power to revoke the trust at any time. H, however,

promises that if he revokes the trust he will transfer to W property in the value of $100,000. The transfer in trust and the agreement were not incident to divorce, but some years later W divorces H. The court decree is silent as to alimony and the trust. After the divorce, income of the trust which becomes payable to W is taxable to her, and is not taxable to H or deductible by him. If H later terminates the trust and transfers $100,000 of property to W, such $100,000 is not income to W nor deductible by H.

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